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Message Text

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ACTION EUR-25

INFO OCT-01 ISO-00 SSO-00 NSCE-00 INRE-00 CIAE-00 PM-07

INR-10 L-03 NEA-10 NSAE-00 PA-04 RSC-01 PRS-01 SPC-03

USIA-15 TRSE-00 SAJ-01 ACDA-19 SS-20 NSC-10 EB-11

OMB-01 DODE-00 DRC-01 ABF-01 /144 W
---------- 121435
O R 141123Z NOV 73
FM AMEMBASSY BONN
TO SECSTATE WASHDC IMMEDIATE 8705
INFO USMISSION NATO BRUSSELS
CINCUSAREUR HEIDELBERG
CINCUSAFE RAMSTEIN
CINCEUR VAIHINGEN

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FOR UNDER SECRETARY CASEY: DEPARTMENT PLEASE ALSO
PASS TREASURY AND DEFENSE

E.O. 11652: GDS
TAGS: EFIN, GW
SUBJECT: OFFSET AND JACKSON/NUNN

REF: USNATO 5437

1. SUMMARY: THE CURRENT STATUS OF THE GERMAN AND NATO OFFSET/BURDENSHARING NEGOTIATIONS INDICATE THAT WE WILL BE ABLE FORMALLY TO MEET THE JACKSON/NUNN OFFSET REQUIREMENTS BY OBTAINING ENOUGH HARD OFFSET DURING US FY 74 AND 75 COMBINED FROM OUR EUROPEAN NATO ALLIES TO OFFSET FY 1974 US MILITARY BALANCE OF PAYMENTS EXPENDITURES IN EUROPE. IN OUR VIEW THE NEGOTIATIONS ALSO SHOW THAT THERE IS NO CHANCE OF INCREASING HARD OFFSET TO SUCH AN EXTENT AS TO OFFSET FULLY IN ONE YEAR THE FY 1974 US MILITARY BALANCE OF PAYMENTS OUTFLOW. AS WE SEE IT, OUR ALTERNATIVES THEREFORE ARE EITHER TO
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ACCEPT A TWO YEAR HARD OFFSET FOR ONE YEAR'S

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EXPENDITURES AND IN THE MEANTIME WORK WITH THE CONGRESS -- HOPEFULLY AGAINST THE BACKGROUND OF SUBSTANTIAL SURPLUSES IN THE OVERALL US BALANCE OF PAYMENTS -- FOR A NON-REPETITION OR SUBSTANTIAL MODIFICATION OF THE NUNN/JACKSON AMENDMENT OR, ALTERNATIVELY, TO ACCEPT LOANS IN THE OFFSET TO FILL THE GAP. IF WE DECIDE TO GO FOR LOANS, WE BELIEVE THAT THE PROSPECTS ARE FAIRLY GOOD OF PERSUADING THE GERMANS TO COME THROUGH WITH SUFFICIENT LOANS TO MAKE IT UNNECESSARY TO APPROACH OTHER NATO PARTNERS FOR FINANCIAL OFFSET PROVIDED WE AGREE TO ACCEPT THE TRADITIONAL 20 PERCENT FLOW-BACK ASSUMPTION. WHILE THE GERMANS PROBABLY COULD BE PERSUADED TO INCLUDE SOME INTEREST RATE SUBSIDY WITH SUCH LOANS, THE TERMS AND CONDITIONS NEVERTHELESS WOULD IN ALL LIKELIHOOD FALL VERY FAR SHORT OF WHAT WE WOULD CONSIDER TO BE DESIRABLE. WE SUGGEST THAT WE SEEK TO CONCLUDE THE NEGOTIATIONS QUICKLY, PERHAPS AIMING AT THE NATO MINISTERIAL MEETING IN BRUSSELS IN MID-DECEMBER. END SUMMARY.

2. THE CURRENT STATE OF THE NEGOTIATIONS INDICATE PROSPECTS OF HARD OFFSET FOR FY 1974 AND FY 1975 COMBINED ALONG THE FOLLOWING LINES:

(A) CURRENT FRG OFFER OF DM 2,750 MILLION OF MILITARY PROCUREMENT, DM 600 MILLION OF INFRASTRUCTURE (BARRACKS, ETC.), DM 180 MILLION URANIUM ENRICHMENT AND DM 20 MILLION OF TAX AND LANDING FEE PAYMENTS MAKING A TOTAL OF DM 3.5 BILLION OR $1.4 BILLIO AT THE DM 2.50 PER DOLLAR EXCHANGE RATE WE ARE USING FOR ALL CONVERSIONS IN THE GERMAN NEGOTIATIONS (USE OF A DIFFERENT EXCHANGE RATE WOULD PROBABLY NOT CHANGE THE RESULTS SIGNIFICANTLY SINCE IT WOULD AFFECT EQUALLY BOTH THE CONVERSION INTO DOLLARS OF OUR DM EXPENDITURES AND THE GERMAN OFFSETTING PAYMENTS).

(B) AS INDICATED IN PARA 2 OF REFTEL THE OTHER EUROPEAN NATO PARTNERS ARE CURRENTLY EXPECTED TO MAKE DURING FY 1974 MILITARY EXPENDITURES RESULTING IN US BALANCE OF PAYMENTS RECEIPTS OF $522 MILLION. WE UNDERSTAND THAT THESE MAY BE INCREASED SOMEWHAT BY COUNTING, PARTICULARLY IN THE CASE OF ITALY, PROCURE-

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MENT IN THE US OF MILITARY EQUIPMENT THROUGH COMMERCIAL CHANNELS AS WELL AS BY SOME PROMISED INCREASES BY THE UK AND OTHERS (SEE PARA 3 OF REFTEL). OFFSETTING EXPENDITURES BY THE EUROPEAN NATO ALLIES OTHER THAN GERMANY THUS ARE LIKELY TO AMOUNT TO AB OVE $1.2 BILLION DURING THE TWO YEAR PERIOD (I.E., $600 MILLION PER YEAR).

(C) HARD OFFSET BY ALL EUROPEAN NATO COUNTRIES

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COMBINED THUS CURRENTLY CAN BE EXPECTED TO AMOUNT TO
APPROXIMATELY $2.6 BILLION DURING US FY 1974 AND 1975
COMBINED AND THUS MORE THAN OFFSET THE ESTIMATED
$2.3 BILLION US MILITARY EXPENDITURES.

3. ON A ONE YEAR BASIS, ON THE OTHER HAND, THE
CURRENT STATE OF THE NEGOTIATIONS INDICATES HARD OFFSET

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OF ABOUT $1.3 BILLION (I.E., HALF THE TWO YEAR TOTAL)
AGAINST EXPENDITURES OF $2.3 BILLION. IT MIGHT BE
POSSIBLE TO REDUCE THE EXPENDITURES SOMEWHAT BY A
REDISTRIBUTION OF SHARES IN NATO MILITARY, CIVIL AND
INFRASTRUCTURE BUDGETS (SEE PARA 3 REFTEL). IT MIGHT
ALSO BE POSSIBLE TO UP THE HARD OFFSET SOMEWHAT MORE,
BUT NEVERTHELESS A GAP OF AB OUT $800-900 MILLION WILL
REMAIN. IF, HOWEVER, WHOEVER JUDGES THESE MATTERS IN
TERMS OF JACKSON/NUNN AGREES FOR NATO AS A WHOLE TO
ACCEPT THE 20 PERCENT FLOW-BACK CONCEPT (AS WELL AS THE
BARRACKS REHABILITATION) WHICH WE HAVE TRADITIONALLY

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ACCEPTED IN US/GERMAN OFFSET NEGOTIATIONS, THE GAP WOULD BE REDUCED BY $460 MILLION (20 PERCENT OF OUR $2.3 BILLION EXPENDITURE FIGURE). WE BELIEVE THE GERMANS COULD BE PERSUADED TO FILL THE REMAINING GAP OF $340-440MILLION BY LOANS WHICH WOULD CONTAIN SOME CONCESSIONAL ELEMENTS. (IN THE US/GERMAN OFFSET AGREEMENT THIS WOULD IMPLY $880 MILLION OF LOANS.) WE WOULD CAUTION, HOWEVER, THAT IT IS VERY UNLIKELY THAT THE GERMANS WOULD BE PREPARED TO SUBSIDIZE THE INTEREST
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RATE BY MUCH MORE THAN A COUPLE OF PERCENTAGE POINTS AND WOULD FIND IT DIFFICULT TO MEET OTHER ASPECTS OF THE TERMS AND CONDITIONS WE MIGHT DESIRE.

4. WE REALIZE THAT LOANS IN THE OFFSET ARE PROBLEMATIC AND THAT THE 20 PERCENT FLOW-BACK IS DEBATABLE IN TERMS OF JACKSON/NUNN. REALISTICALLY, HOWEVER, WE BELIEVE THESE ARE THE ONLY ALTERNATIVES TO THE ONE FOR TWO YEAR APPROACH OUTLINED IN PARA 2.

5. NEGOTIATION OF OFFSET ARRANGEMENTS UNDER EITHER ALTERNATIVE SHOULD, WE FEEL, BE CONCLUDED AS QUICKLY AS POSSIBLE. WE MIGHT AIM TO WRAP UP THE AGREEMENT IN BRUSSELS AT THE MID-DECEMBER NATO MINISTERIAL SESSION, AS WE DID IN 1971, AND STEP UP NEGOTIATIONS AS REQUIRED. IT WOULD BE WORTH A LOT OF EFFORT TO GET THIS IRRITANT IN OUR RELATIONS RESOLVED RIGHT AWAY, AND NOT LET IT DRAG ON INTO 1974.

6. WHILE THE FOREGOING SOLUTIONS DO NOT RESOLVE THE BURDEN-SHARING ISSUE, WE BELIEVE THEY WOULD IN EITHER CASE PAVE THE WAY FOR AN OBJECTIVE MULTILATERAL BURDEN-SHARING NEGOTIATION. THE GERMANS COULD PLAY A MUCH MORE CONSTRUCTIVE ROLE WITH THE BILATERAL OFFSET AGREEMENT BEHIND THEM AND IN THE ASSURANCE OF A HEALTHY BURDEN-SHARING CREDIT. CLEARLY ALSO, THEIR SUBMISSION OUTLINING THE BURDEN THEY ALREADY BEAR, INTER ALIA, IN FINANCING BERLIN FORCES AND PROVIDING FREE LAND AND FACILITIES, WILL REQUIRE CAREFUL EXAMINATION. WE HAVE OMITTED THIS FRG PROPOSED ELEMENT FROM OUR OFFSET SOLUTION POSSIBILITIES SINCE WE CONSIDER THIS TO BE A FACTOR IN BURDEN SHARING AND NOT IN OFFSET. IN FACT, WE MAY FIND THAT OUR EXTRA BUDGETARY COSTS ATTRIBUTABLE TO STATIONING OUR FORCES IN THE FRG RATHER THAN IN THE US ARE LESS THAN WE HAD ESTIMATED.
HILLENBRAND

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